bargaining power over the cable operators. They could insist on a high fee for their national networks or they could negotiate for carriage of other programming. Must-carry and retransmission were government granted rights of carriage, means of ensuring access to audiences. The broadcasters chose to bargain for more channels on cable systems, rather than charge for their broadcast networks.

The 1'996 Telecommunications Act reinforced this process. The Act allowed the FCC to lift the ban on horizontal concentration in the television industry. Broadcast licenses had been limited to one per entity in each market. The 1996 Act allowed the FCC to award more than one license per market after it had considered its impact on the industry. The FCC chose to allow duopolies in markets in which there would he at least eight "voices" in the market after the merger of two stations. Generally, the largest markets were opened to duopolies under the reasoning that diversity would be preserved in those markets.

For independents that sold product into TV syndication, this change had the opposite effect. By allowing the broadcast networks to own **two** stations in the most important markets – especially New York, Chicago and Los Angeles – a second major outlet was pulled into the tightening, vertically integrated core. The new owners of the second station now had a great deal of content of their own since, over the course of a decade, every major network acquired one of the major studios. Vertical integration became complete. Syndication was more difficult because access to the most important markets became much more difficult.

STRATEGIC MOVES

These changes did not take place instantaneously, but unfolded over a number of years for several reasons. When a policy change takes place, it frequently *takes* a period of time for regulators to implement legislated requirements. Parties will frequently litigate such changes and move slowly until the legal terrain is clear. Further, existing business relations must unwind Contracts run their course and new models are developed. Finally, because many of these policies are highly visible political. decisions, market participants try to avoid triggering a political reaction with **extreme** moves.

The 1990s policy changes triggered a series of acquisitions and product developments over the course **of** the decade that created a vertically integrated oligopoly in the television industry **(see** Exhibit 111-2).

Exhibit III-2:
Major 1990s Acquisitions and Launches Involving Broadcasters in the Creation of the Vertically Integrated Video Entertainment Oligopoly

Year	Disney/ABC	Time Warner	Viacom/CBS	G.E-NBC	Fox
1993		Turner acquires Castle Rock & New Line:			**Fox** acquires NFL rights
1994			Viacom acquires Paramount		
1995		Time Warner launches WB	CBS launches UPN		
1996	Disoey acquires ABC	Time Warner acquires Turner			
1999			CBS acquires King World Viacom acquires CBS	NBC acquires **30%** of Paxson	
2001					**Fox** duopolies **LA,** Minn. DC Houston
2002				NBC acquires Telemundo NBC duopolies **result**	**Fox** duopolies Chic. Orl.
2003				**GE** Acquires Universal	

Source: Columbia Journalism Review, ***Who Owns What,* August** 22,2006.

Most directly, the networks could monopolize access to audiences in prime time broadcast television, foreclosing the streams of revenue that sustain production of all forms of content. Within a decade, the amount of programming on prime time owned by the networks increased dramatically, from 15% to around 75%. First the independents were excluded from prime time.$@ then the major studios were absorbed.

'Each of the big three networks merged with a major studio and acquired cable programming over the course of the 11990s. Fox had taken a different path to vertical integration. After being rebuffed in an effort to acquire Warner studio, News Corp. acquired Twentieth Century Fox and a number of television stations in major markets, both in 1985.
Since the late 1970s, Twentieth Century Fox had been one of the least active of the major studios in providing television programming,. Fox's focus through the 1990s would not be on original programming as traditionally defined for prime time. It would focus on sports in programming and broadcast duopolies.

Interestingly, Fox was vertically integrated but remained below the threshold for being subject to the Fin-syn rules. For the big three networks who were subject to the rules, the repeal of Fin-syn made mergers between networks and studios profitable, as self-supply was now allowed.

THE CURRENT STATE OF THE 'VIDEO PRODUCT ENTERTAINMENT SPACE

Vertical Integration

Within less than a decade after repeal of Fin-syn and the passage of the 1996 Telecommunications Act, the process of vertical integration and horizontal consolidation was complete. This paper defines vertically integrated entities at the core of domestic video entertainment as the five firms that, in the past decade, have come to own major studios, broadcast networks and cable TV channels while holding television station licenses as well (see Exhibit III-3). The names are familiar to all in both the television and the theatrical movie space. All of the entities have a presence in each of the major video entertainment areas – network television, cable television and movie production. These firms account for five of the seven studios that produce motion pictures – known as the majors.

The depiction and data in Exhibit III-3 are for the early 2000s. While there have been some changes in the direction **of** deintegration that movement is not complete and its implications are not yet clear. CBS and Viacom have become partially separated. They still share the same Chairman (Sumner Redstone). Each **of** the **two** potential entities is vertically integrated on its own, with distinct production and distribution facilities. Similarly, **Fox** and Liberty remain precariously intertwined by substantial ownership of shares, although an exchange and separation of ownership in **Fox** and DirecTV may be in the offing. These evolving situations may change the landscape somewhat, hut the distribution arrangement made by the separate entities would still reflect the legacy of vertical integration. Thus, we may see these entities unwind toward truer deintegration and independence, although the history of Liberty teaches that spin-offs and pull-backs are entirely possible. Moreover, whether these developments will constitute a true opening of the field to independents, or whether these entities will simply substitute contractual relationships to duplicate the integrated flow of content, also remains to be seen. **Nor** is it clear that **the** parts that have been broken up will not use their remaining partially integrated assets (production and distribution) to reintegrate across

Exhibit 111-3:
The Vertically Integrated, Video Entertainment Oligopoly

Parent	Television Property	Cable/Satellite	Film Production
News Corp.	**35 TV** Stations reach **39%** of U.S. Households **9** duopolies – **N.Y.** L.A. Chic. Minn. D.C. Dallas, Phoenix, Orlando, Houston Fox Network	Fox News, Fox Movie FX, FUEL, Nat. Geog. Speed, Fox Sports, Regional Sports, College, Soccer DirecTV	**20th** century FOX, Fox Searchlight, Fox Television S, Blue Sky Studios
General Electric	**28** TV stations reaching **34% of U.S** households *6* duopolies through Telemudo – NY, LA, Chic., SF, Dallas, Miami NBC Network *30%* of Paxson	CNBC, MSNBC, Bravo, Sci-Fi, Trio, USA	Universal
Disney	**10 TV stations reaching** **24% of U.S. households** **ABC Network**	ESPN, ABC Family, Disney Channel, Toon Disney Soapnet, Lifetime A&E	Walt Disney Touchstone Hollywood Buena vista Pixar Miramax
CBS/Viacom	**17** TV stations reaching **39%** of U.S. households CBS Network CW King World	Showtime MTV, Nickelodeon BET, Mick at Night TV land, Noggin Spike TV, CMT Comedy Central, Flix The Movie Channel Sundance	Paramount Paramount Home
Time Warner	CW Network	HBO, **CNN,** Court TV, Road Runner New York News 1 Time Wamer Cable **14.5** million subscribers	Warner Bros. Studios, TV Home Video Domestic Pay-TV Telepictures, Hanna- Barhera Witt-Thomas,

Source: Columbia Journalism Review, ***Who* Owns *What,*** August **22,2006.**

the entire space.[26] The effects of any real de-integration, if it comes about, will play out over time.

Note that each of the entities has a presence in all of the key areas of video production and distribution. Each owns studios that produce video product for both television and theatrical release. Each has substantial ownership of television distribution. The four national broadcast networks are represented here. The broadcasters have substantial ownership of TV stations. The fifth entity, Time Warner, is a major cable operator. As a result of the recent Adelphia acquisition and exchange of cable systems with Comcast, Time Warner dominates the two entertainment centers in the **U.S.,** New York and Los Angeles. It also has a share in the new broadcast network, CW, to which its production operations are providing content.

Each of the five also has substantial cable offerings. Indeed **24** of the top 25 cable channels, as measured by homes passed, are owned by these five entities. In terms of actual viewers, as opposed to homes where programming is available, these five entities account for the vast majority – as much as 85 percent -- of prime time viewing.

Horizontal Concentration

Reflecting this concentration of subscribers, viewers and facilities, these five, vertically integrated entities have come to dominate the domestic U.S. video entertainment product space (see Exhibit III-4). They accounted for about three quarters to four-fifths **of** the output of the video product in terms of writing budgets, programming expenditures, hours of prime time content, and domestic theatrical box office or video sales/rentals.

[26] Grove, Martin **A., "CBS'** Moonves Smart to Eye Movies," *Hollywood* ***Reporter.com.*** July 7, **2006.**

Exhibit III-4: Vertically Integrated Video Oligopoly Domination of Television and Movie Production and Distribution
(Circa 2001-2003)

	TELEVISION							MOVIES/DVD (US Rev)	
	Subscribers*		Writing Budgets		Programming Expenditures		Share of Prime Time	Box Office	Video
	# Million	%	$ Million	%	$ Million	%	%	%	%
FOX/LIBERTY	1250	21	236	19	3803	9	3	11	10
TIME WARNER	925	15	206	17	7627	18	10	22	20
CBSMACOM	910	**15**	45	12	9555	22	**28**	**8**	7
ABCDISNEY	705	12	132	**11**	6704	16	**21**	20	22
NBC/Universal**	720	12	159	13	3879	9	21	12	15
Subtotal	4315	75	772	72	31568	74	83	73	74
TOTAL	6000	100	1225	100	43212	100	100	**100**	**100**
HHI		**1179**		**1084**		**1226**	**1775**	**1213**	**1258**
FOUR FIRM CR		**63**		**61**		**65**	**70**	**65**	***61***

Notes and sources: * Subscribers includes broadcast and cable homes passed. ** Universal added to NBC to project post-merger market. Federal Communications Commission, In the Matter of Annual Assessment of the Status of Competition in Markets for the Delivery ad Video Programming, CC Docket No. 00-132, Seventh Report, Tables D-1, D-2, D-3, D-6, D-7; Television Market Report: 2001 (Washington, D.C.: BIA Financial Network, 2001); Comments of the Writers Guild of America Regarding Harmful Vertical and Horizontal Integration in the Television Industry, Appendix A. Federal Communications Commission, In the Matter of Implementation of Section 11 of the Cable Television Consumer Protection and Competition Act of 1992; Implementation of Cable Act Reform Provisions of the Telecommunications Act of 1996The Commission's Cable Horizontal and Vertical Ownership Limits and Attribution Rules Review of the Commission's Regulations Governing Attribution Of Broadcast and Cable/MDS Interests Review of the Commission's Regulations and Policies Affecting Investment In the Broadcast Industry, Reexamination of the Commission's Cross-Interest Policy, CS Docket No. 98-82, CS Docket No. 96-85, MM Docket No. 92-264, MM Docket No. 94-150, MM Docket No. 92-51, MM Docket No. 87-154, January 4, 2002; Bruce M. Owen and Michael G. Baumann, "Economic Study E, Concentration Among National Purchasers of Video Entertainment Programming," Comments of Fox Entertainment Group and Fox Television Stations, Inc., National Broadcasting Company, Inc. and Telemundo Group, Inc., and Viacom, In the Matter of *2002* Biennial Regulatory Review – Review of the Commission's Broadcast Ownership Rules and Other Rules Adopted Pursuant to Section 202 of the Telecommunications Act of 1996, Cross Ownership of Broadcast Stations and Newspapers, Rules and Policies Concerning Multiple Ownership of Radio Broadcast Stations in Local Markets, Defmition of Radio Markets, MB Docket No. 02-277, MM Dockets 02-235, 01-317, 00-244, January 2,2003; Federal Communications Commission, Program Diversity and the Program Selection Process on Broadcast Network Television, Mara Epstein, Media Ownership Working Group Study 5, September *2002*, pp. *26;* David Waterman, Hollywood's Road to Riches (Cambridge: Harvard University Press, 2005), pp. 21, 25.

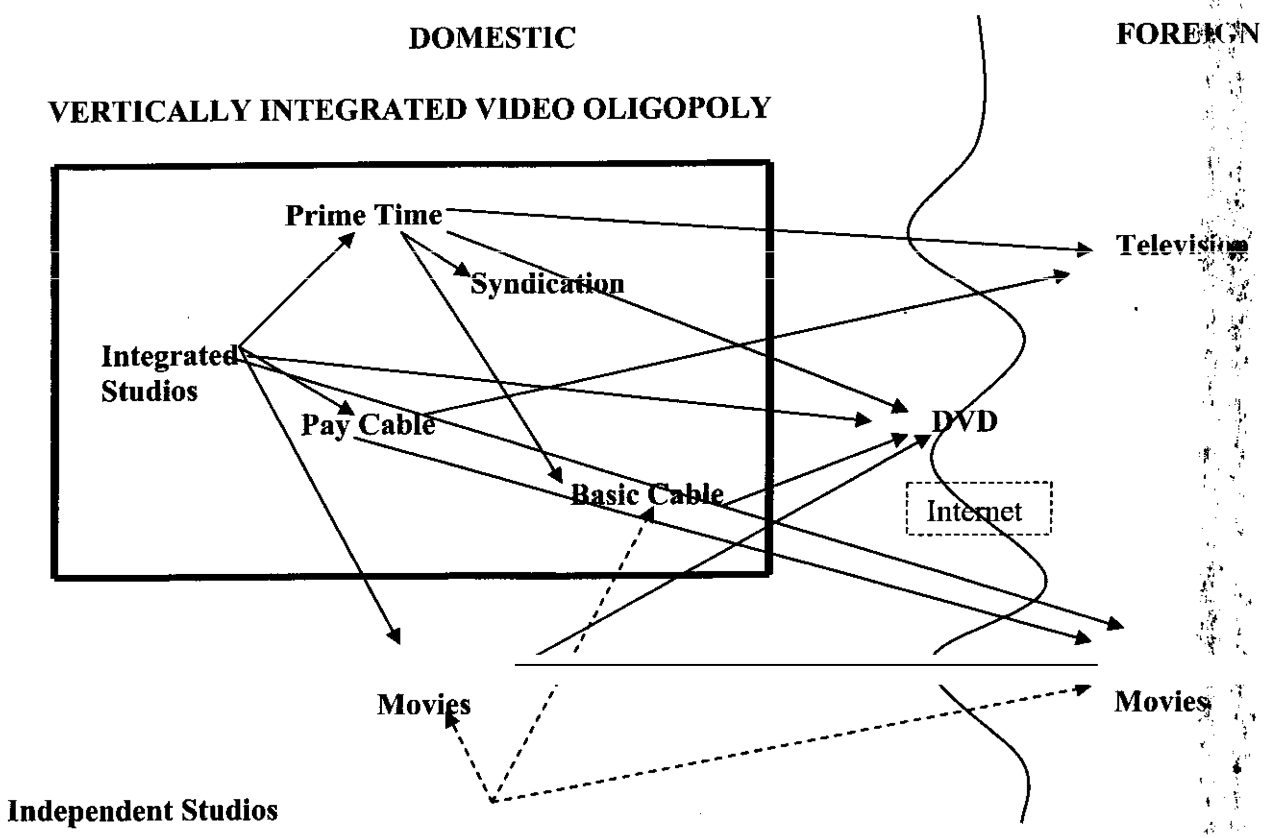
In each case, the HHI is in **the** concentrated range and the four **firm** concentration ratio is in the tight oligopoly range. The two potential changes in the sector noted above would not change this basic finding. Each of the measures of concentration would likely remain in the concentrated tight oligopoly range.,but ***the*** identity of the leading firms might change a bit.

The broadcast space at the core of the vertically integrated oligopoly is extremely important to the overall market for video product ***(see*** Exhibit III-5). Where a program or film is placed in television space strongly affects not only its domestic revenues, but has a large impact on where it will be placed and what revenues it can earn in **the** international arena. By foreclosing the broadcast space, for both movies and **series,** the oligopoly core cripples independent producers and forces them into the cable arena, insofar as the independents desire to distribute over the television platform. The cable space, though, is a hostile environment as well, wherein the very same entities own the most attractive distribution channels in the space. Independents are forced into the least attractive cable channels on the least favorable terms.

THE CONDITIONS FOR THE EXERCISE OF MARKET POWER

Thus, the basic conditions for public policy concern about the potential exercise of market power are present. The empirical analysis demonstrates key economic characteristics of **the** video entertainment product space. It is a moderately to highly concentrated, tight oligopoly that is vertically integrated in production and distribution and exercises monopsony power – control and market power over the purchase of programming from independents.

Exhibit III-5:
Location in the Domestic Exhibition Space Strongly Influences Prospects in Foreign Markets



The remainder of this analysis presents evidence that market power has been exercised. In the process of creating the vertically integrated oligopoly, these entities behaved in a manner that created their market power through mergers, acquisitions and product development and exploited their market power through self-dealing, foreclosure of markets and imposition of onerous terms and conditions on suppliers. The key elements of the video entertainment product space include:

Market structure and market power

- Market shares that have risen to the level traditionally defined as a source of concern about concentration setting the stage for the abuse of market power.
- Substantial barriers to entry in the industry.
- **A** history of anticompetitive practices.

Vertical Integration

- Barriers to entry increased by vertical integration.
- The foreclosure of markets to unaffiliated producers through favoritism of affiliated upstream production and the subsequent exit of upstream, unaffiliated product suppliers from the market.
- Parallelism and reciprocity among the dominant firms in the oligopoly.
- **A** rush to integrate and concentrate across the sector.

Monopsony Power

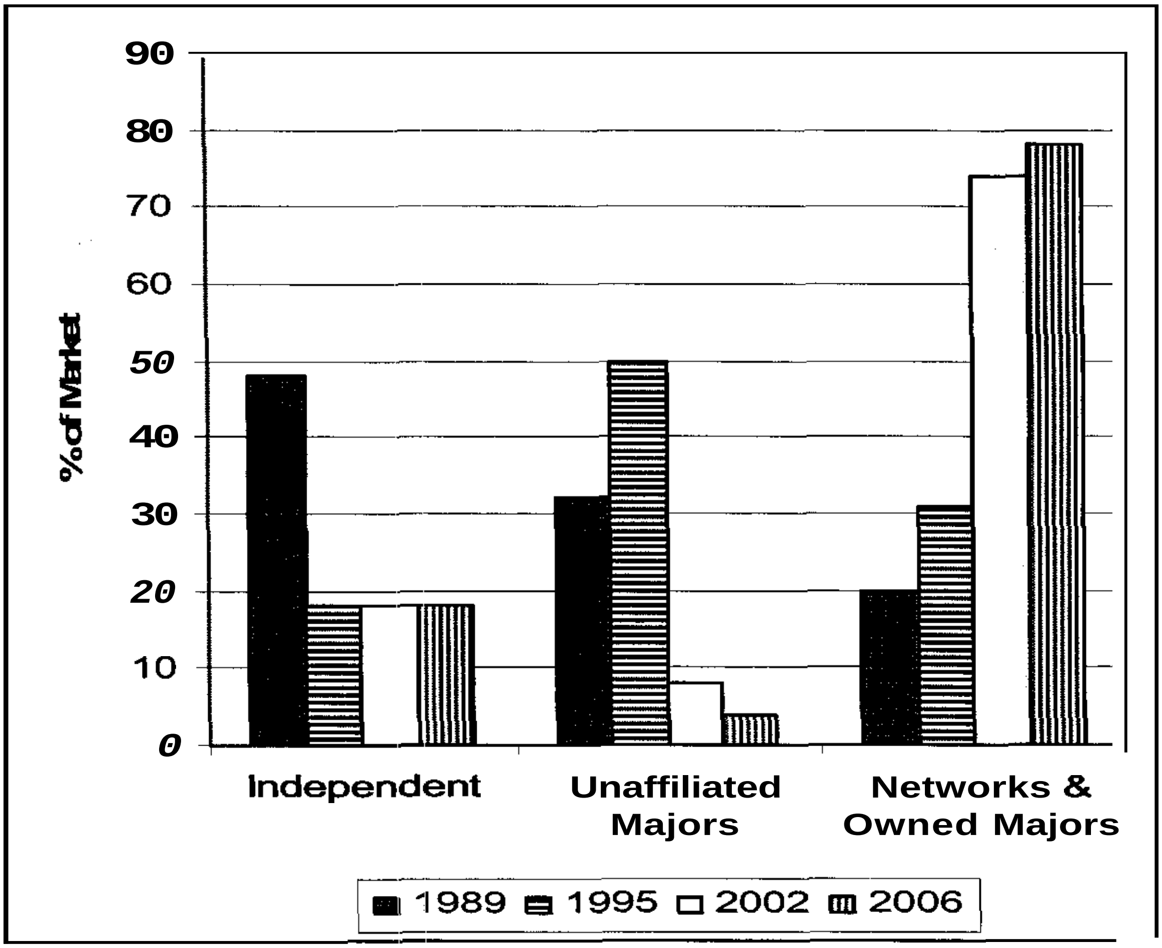
- The imposition of prices that squeeze unaffiliated producers and terms that shift risk onto those producers.
- Indications of a decline of quality in product attendant on the abuse of monopsony power.
- Flooding of downstream outlets with integrated product.

IV. DOMINATION OF THE TELEVISION PRODUCT SPACE

PRIME TIME ON BROADCAST/NETWORK TELEVISION

The central empirical fact at **the** core of the narrative of the 1990s is **the** dramatic and swift change in the ownership of prime time programming after the repeal of the Fin-Syn **rules** ***(see*** Exhibit IV-1). Studies of prime time programming just **prior** to the repeal of the

Exhibit IV-1:
Prime Time Market Shares



Source: 1989-2002 calculated from Mara Einstein, ***Media Diversity: Economics, Ownership and the FCC*** (Mahwah Lawrence Erlbaum, 2004), p 169; 2006 based on Baseline Research, ***Fall Television Schedule: 2006-2007 Season.***

Fin-Syn rules find that the networks owned around 15 percent of shows aired in prime time. Major studios owned about one-Third and independents accounted for about a half. Within five years, the role of the independents had been dramatically reduced – to less than one-fifth of the programming. Networks had grown to almost 40 percent. The major studios still accounted for around 40 percent. The mergers of the networks and studios followed and the vertically integrated entities came to dominate prime time, accounting for over three quarters of the programs. In 1989, fifteen entities produced 2 percent or more of the programming on prime time. By 2002, that number bad shrunk to five. The programming produced by independents in 2006 was largely reality shows, not scripted programming, as had been the case in the recent past.

Traditional measures of market concentration used in economic analysis reinforce this observation. **As** Exhibit IV-2 shows, the prime time market moved very quickly from an unconcentrated competitive market (CR4=34%; HHI=541) to a tight oligopoly (CR4=74%) **well** up into the moderately concentrated range (HHI=1596). If the calculations are based only on series, i.e. excluding movies, the concentration is even greater. Within a decade after

Exhibit IV-2:
Concentration of Prime Time Programming

Year	Four Firm Concentration	HHI	Four Firm Concentration	HHI
All Prime Time Hours			***Series** only*	
1989	35	541	40	703
1995	47	716	57	1165
2002	74	1596	84	2070

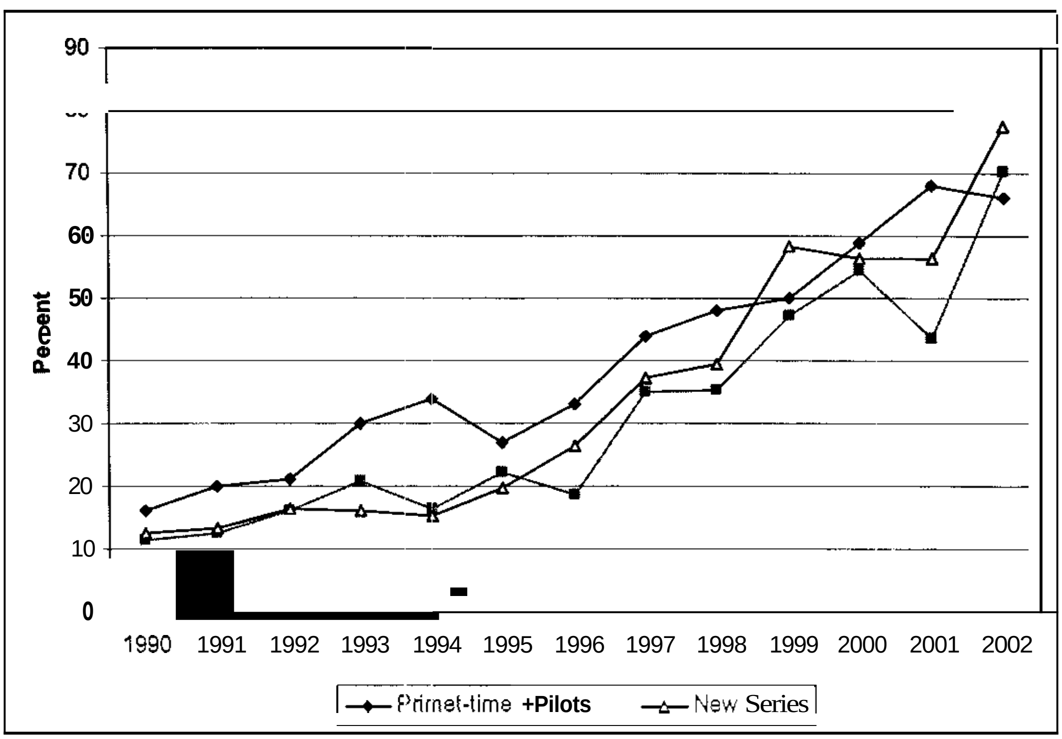
Source: Calculated from Mara Einstein, ***Media Diversity: Economics. Ownership and the*** FCC (Mahwah: Lawrence Erlbaum, 2004), p. **169.**

the repeal **of** Fin-syn, the market 'was a highly concentrated (HHI=2070) tight oligopoly (CR4=84).

NEW SHOWS AND PILOTS

Exhibit IV-3 shows the pattern of ownership by the networks of prime time programming, new shows and pilots;. We observe a modest increase in network ownership in the early 1990s, as the Fin-syn ruler; were partially repealed, debated and litigated. With final repeal of the rules in 1995, we *see:* a rapid and steady increase in network ownership.

Exhibit IV-3:
Network Ownership of Prime-Time Programming 1990-2002



Source: Calculated from Mara Einstein, *Media* ***Diversity: Economics, Ownership and the*** FCC (Mahwah Lawrence Erbium, 2004), p. 171; William T. Bielby and Denise D. Bielby, "Controlling Prime Time: Organizational Concentration and Network Television Programming Strategies," *Journal of Broadcasting & Electronic Media,* 47: 4 (2003), **p. 588.**

The pattern has persisted, as an analysis of the 2006-2007 season shows ***(see*** Exhibit **IV-4).** The networks get over half of their programming internally. The four major networks also buy programming from one another. Overall, independents account for **less** than one-**fifth** of prime time programming. On the four major networks, the independents account for about one-seventh. The independent programming is generally reality shows, not scripted programming.

Exhibit IV-4:
Primetime 2006-2007 Programming
(Percent of Hours)

	Self-Dealing,	Internal Big-5 Dealing	Sony	Independents
ABC-Touchstone	**52**	**20**	**3**	**25**
CBS-Paramount	**57**	**38**	**0**	**5**
NBC-Universal	**67**	**14**	**5**	**14**
FOX-20th Century	**52**	**29**	**6**	**13**
CW-Warner/ Viacom	**53**	**0**	**7**	**40**
Total	**57**	**21**	**4**	**18**

Source: **Baseline** Research, ***Full Television Schedule: 2006-2007 Season***

SYNDICATION

Syndication has been **studied less** than prime time, but **the** available data suggests a similar pattern ***(see*** Exhibit IV-5) Although there is less self-dealing, **the** five networks dominate the syndication market because of a large amount of internal dealing. Particularly interesting to note is the lack of recent independent shows in syndication. Having been forced out of prime time, independents simply do not have **series** to place as product in syndication.

Exhibit IV-5:
Self-Dealing and Internal Dealing in First-Run Syndicated Programming (2004)

TYPE OF TRANSACTION	HOURS All Shows	HOURS Shows Less Than 2 Years Old
Self-Dealing (Subsidiaries of Big 5 syndicating to themselves)	32%	61%
Internal Dealing (Subsidiaries of Big 5 syndicating to Big 3 station groups)	41	16
Independents syndicating to Big 3 Station Groups	18	0

Sources and Notes: Calculated from Goro Oba and Sylvia M. Chan-Olmstead, "Self-Dealing or Market Transaction?: An Exploratory Study of Vertical Integration in the U.S. Television Syndication Market," *Journal of Media Economics*, 19(2), 2006, p. 113.
Big 3 station groups are CBS/Viacom, Fox and ABC
Big 5 syndicators are King World, Paramount, 20" Century Fox, Buena Vista, WB and Universal. Other Major is Sony (Columbia). Independents are "other."
There are 22.5 hours per week of first-run syndicated programming in the 9am to 8pm day part analyzed (77 hours).

The foreclosure of the broadcast/network television market, particularly for 1st run series, is reinforced by a complete lack of pilots coming from independents. Interviews with independent producers done for this paper reveal that since there is little chance that they will get on the air, they have abandoned this market.

I have noted that the decision to allow broadcasters to hold multiple licenses in a single market contributed to the difficulties of independents gaining access to the syndication market. The network owners would use their internally produced content on the television stations in the largest markets, squeezing the space available to unaffiliated producers. About 75 duopoiies were created soon after the ban on holding multiple licenses was lifted. The national networks concentrated their duopoly acquisitions in the top ten markets, even though owning multiple stations within a market did not count against the national cap on how many homes they were allowed to reach. These markets account for about 30 percent of all **the** TV households in the country and almost 40% of all the TV revenues in the country. The big four network's market share in the top three markets was particularly high. These three markets alone account for about 15 percent of the population and almost 20 percent of TV revenues in the nation.

Exhibit VI-6:
Big 4 Network Duopolies and Market Share in Top 10 Markets

Designated Market Area	*Number of Big 4 Duopolies*	*Market Share Big 4 Duopolies*	*Total Market Share of Big 4*
New York	2	44	77
Los Angeles	3	62	79
Chicago	2	40	73
Philadelphia	1	25	57
San Francisco	2	37	56
Boston	1	28	42
Dallas	3	59	59
Washington D.C.	1	21	52
Atlanta	0	0	24
Detroit	1	24	42

Source: BIA Financial, *Television Market Report, 2003*

TV MOVIES, THE ROLE OF CABLE

The history of prime time programming is primarily a story about television series. While a small number of made for TV movies appear in prime time, the overwhelming majority of programming is series. Interestingly, for independents, the growth of cable in the late 1990s was a story about TV movies.

To analyze the changing patterns of TV movies, **I** examined all films aired in **three** four-year periods *(see* Exhibit IV-7. The first period was before the Fin-syn rules were in play (1985-1988). The second period was the four **years** after Fin-syn was repealed (1995-1998). The third period was after the networks became integrated with studios (2001-2004).

Exhibit IV-7
TV Movies Across All Distribution Channels

	Percent of Movies		
	Broadcast	***Basic Cable***	***Premium Cable***
1985-1988 (n=47)			
Independent	39	0	2
Network	47	2	2
Majors	9	0	0
1995-1998 (n=206)			
Independent	33	13	16
Network	18	1	5
Majors	11	0	2
2001-2004 (n=634)			
Independent	7	41	9
Network	5	20	7
Majors	5	5	1

Source: **Baseline Beta** Studio System **Database**.

I relied on the baseline database and included only movies that were aired and for which a network and at least one producer was identified. Where **a** network was listed as **a** producer, the movie was considered to be produced by the network, even if other (unaffiliated) producers were identified. This is the critical assumption in the *sense* that I **am** assuming, implicitly, that the movie would not have been aired on the network, but for the network's interest in **the** co-production. Of lesser importance is **the** assumption that where a network and its major movie studio are both listed as producers, the studio was considered to be the producer. While these distinctions could be interpreted in other ways, the basic patterns in the data would not change much. The key findings about independent producers are quite clear (as shown in Exhibit IV-7).

The pattern of broadcast movies follows the pattern we observed for series. The independents played a large role under Fin-syn, were diminished immediately after the repeal of Fin-Syn and then reduced dramatically within a decade. Their share in premium movies grew in the mid-1990s, but was reduced after the integration of the studies.

In the most recent period, cable movies have become quite prominent. The numbers of movies produced have increased dramatically. In the mid-1990s, independents aired about 120 movies, 95 of them on broadcast and premium cable. In the 2001-2004 period, they produced over 100 movies on broadcast and premium cable, and over 260 on basic cable. The apparent increase in production, however, is less significant than it appears. There are two different sets of reasons that the expansion has not helped independents greatly. One set has to do with the nature of the business and the distribution channels.

First, broadcast and premium movies have much higher budgets and larger audiences. Thus, the 100 movies produced by independents that aired on broadcast and premium cable probably had a substantially larger total budget and a larger audience than the 260 movies that aired on basic cable.

Second, where studios compete for resources to maintain a production base, the relative output is important. Whereas the independents grew by about 6 percent between the mid 1990s and the early 2000s in the high value spaces, the networks and major studios grew by almost 60 percent. As the networks grew larger and larger, they control more resources in the sector.

Third, placement on basic cable makes it more difficult to tap into other revenue streams – DVD sales/rentals and foreign television – which have become vital to maintaining the program's prominence.

The second set of factors that suggest the growth of basic cable as an outlet is **less** important than it appea to do with the market structure.

First, approximately 80 percent of the basic cable movies aired in the **2001-2004** period on networks is now owned by two of the vertically integrated media corporations – ABC/Disney (ABC family, Disney Channel and Lifetime) and NBC (Sci-Fi).

Second, **the** genres are highly specialized. These cable networks buy three genres, each with a respective dominant buyer. ABC Family/the Disney Channel buy family/children-oriented movies. Lifetime buys romances. Sci-fi buys science fiction films. This is a classic situation for the exercise of monopsony power.

Third, the vertically integrated oligopoly that dominates the other video outlet spaces also thoroughly dominates the TV movie space. The five entities 1have identified as the vertically integrated oligopoly account for about three-quarters of the distribution of movies: one-third through broadcast and premium cable, a little over one-third through basic cable, and another handful on general networks (A&E, MTV, ESPN, FX, Spike).

ACCESS TO TELEVISION IS CRUCIAL TO THE HEALTH OF INDEPENDENT PRODUCERS

Thus, I have shown that **the** independents were largely eliminated from prime time broadcasting and relegated to basic cable movies. This places the independents at a severe disadvantage because television and the broadcast space at the core of the vertically integrated oligopoly remain extremely important to the overall market for video product. Exhibit IV-8 presents order of magnitude estimates of **the** revenues, expenditures and audiences for domestic movie producers and the domestic TV sector. It contrasts cable and broadcast revenues with to sources of revenue for movie producers that **are** 'independent' of the domestic TV sector – domestic **and** foreign theatrical releases and home video sales.

Exhibit IV-8:
The Importance of Television in the Video Entertainment Product Space
(circa 2003-2004)

	MOVIES		TELEVISION		
	Majors	**Independents**		**Broadcast**	**Cable/ Satellite**
Revenues (Billions)					
Domestic			Ad Revenue/ Subscription	$35	$50
Box Office	$ 8.0	$1.0			
Home Video	11.0	1.3			
Subtotal	19.0	2.3			
Foreign					
BoxOffice	8.0	1.0			
Home Video	8.0	.8			
Subtotal	16.0	1.8			
Total	38.3			85	
Programming Budgets (Billions)	7.0	.4		$40	
Audience (Hours Per Year)					
Theatrical	13		Broadcast	780	
Home Video	80		Basic		830
Total	93		Premium		180

Sources: **U.S.** Box Office and Programming budgets are based on MPAA, ***Theatrical Market Statistical Report, 2005.*** Programming budgets do not include marketing and assume 120 releases from the majors. Foreign Box Office, home video and TV revenues are from David Waterman, ***Hollywood's Road io Riches*** (Cambridge: Harvard University Press, 2005), Table C.1. Independent programming budgets from American Film Marketing Association, ***The Economic Impact of Independent File Production.*** April 2003 Cable Revenue is from Federal Communications Commission, ***Twelfth Annual Report in the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming,*** MB Docket No. 05-255, March 3, 2006, p. 19.

The revenue from the TV sector is much larger than the domestic revenue sources for the movie industry – about four times as large – even when video sales/rentals are included. Total revenues from these sources are over two times as large. Even if we were to factor in the domestic and foreign TV revenues **of** movie producers, the domestic TV sector would be almost twice as large.[27]

Programming expenditures of the domestic TV sector are on the order of five to six times as large.

The extreme importance of TV in terms of audience is also clear. Broadcast and cable pull almost twenty times the audience of movies, even combining theatrical and home video viewing. Premium cable (arguably similar to movies since it is a pay service) alone has a larger audience.

Although basic cable and broadcast are about equal in audience, prime time broadcast is still the dominant exhibition space **on** TV. For example, the advance sales of advertising slots on the four national networks – called the up front sales – equals the total annual Box Office of theatrical releases in the U.S. Advertisers pay a rich premium for this space because the networks still aggregate many more viewers than cable shows. As Mara Einstein, the author of the most comprehensive analysis of **the** repeal of the Fin-Syn rules noted, the gatekeeper role of the networks is essential since,

> while the networks must decide between best show versus best buy, they remain acutely aware of their ability to provide something that **no** other media vehicle can, and that is the ability to create a valuable asset because no medium can provide the kind of exposure and promotion that network television does.[28]

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[27] The sources cited in Exhibit IV-8 put this revenue at about **$8** billion.

[28] Einstein, Mara, ***Media Diversity: Economics, Ownership and the FCC*** (Mahwah: Lawrence Erlbaum, 2004), p. 192.

The networks **are** well aware of their advantage. **As** Les Moonves recently put it, "If you want 30 million people, you can't get that anywhere else."[29] The next chapter examines how that gatekeeper role impacted access to distribution under the new policies adopted in the 1990s.

[29] Fabricant, Geraldine and Bill Carter, **"A** Tortoise Savors the Lead," ***New York Times,*** September 12,2006, p. CC11.

V. THE IMPACT OF MARKET STRUCTURE ON INDEPENDENT PRODUCTION

THE CRITICAL ROLE OF GATE KEEPING IN THE VIDEO PRODUCT SPACE

At the center of the picture: I have painted of vertical integration following the policy decisions of the 1990s stand the broadcasters as gatekeepers of access to audiences. A key role in the process was played by the absorption **of** the major studios. Interestingly, David Waterman's recent economic history of the major studios is based on the premise that

> the most important feature of the studios is their role as *distributors,* and we often refer to them by that term. By controlling distribution, the studios act as gatekeepers: they decide which movies get produced and how they are made, and they also largely determine when and at what price viewers get to see them on which media.[30]

The key gate keeping role of distribution in the video entertainment product space was integrated and consolidated with production in single entities in the first 50 years of the movie industry. While there is a debate about the factors that shaped the role of the major studios, Waterman pinpoints two critical issues that parallel the core of my analysis of the video product space in the 1990s. One was a policy decision that forced deintegration.

> **Fox,** MGM, Warner, Paramount, and RKO, known **at** the time as the five majors, were vertically integrated into production and theater exhibition and had consistently dominated the industry since the mid-1930s. The three others – Universal, Columbia and United Artists, known as "the minors" at the time – owned no theaters.. . All eight of these studios were brought to trial by **the** U.S. Justice Department in the 1940s, and an eventual Supreme Court decision in 1948, *United States v. Paramount Pictures, Inc. et al.,* ruled that the eight distributors had violated the Sherman Act and other antitrust laws.. . The Court ordered the five major distributors to divest their extensive theater holdings.. . established a number of regulations on contractual relationships between

[30] Waterman, David, Hollywood's Road to Riches (Cambridge: Harvard University Press, 2005), p. 16.

> distributors and theaters that were incented to level the playing field for independent companies.[31]

The second factor that shaped the market for theatrical movies was the growth **of** television.

> **After** the ***Paramount*** decision, the prewar stability of industry structure among the eight Paramount defendants began to crumble. Industry positions of the majors and the minors converged, and the extent of independent entry increased. We argue in the following chapter that the almost coincident diffusion of television has more profound long-range effects on the movie industry than did ***Paramount,*** but it is likely that ascendance of all three of the minor studios into the majors ranks, and perhaps the **rise *of*** independents in the 1960s, were related to the Court's intervention.[32]

Thus, the policy of forcing deintegration of production and distribution of theatrically released movies opened the door to entry, while the advent of television created a whole new channel for the distribution of video product. Waterman reckons that the technological factor played a large part in shaping the video entertainment space, although not so much in determining concentration **as** in altering the types of products the sector produced and the marketing patterns of those products. However, **from** the point **of** view of the analysis in this paper, the critical point is that the convergence of the same two factors – integration policy and multiple distribution platforms – that worked to weaken the gatekeeper role of the studios in the 1950s, worked in the opposite direction for the broadcasters in the 1990s. Removing the policy restriction on vertical integration opened the door to reintegration of the production and distribution of video product and the merger of production (studios) and distribution (broadcasting and cable). The lesson is clear: if given the chance, entities will merge and integrate vertically in order to dominate the sector by controlling distribution.

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31 Waterman, p. 30.
32 Waterman, p. **23.**

Mara Einstein, already described above as conducting the most thorough investigation of the Financial Interest and Syndication rules, notes that before and after the policy limiting vertical integration the broadcasteirs used their control over access to audiences to monopolize ownership of network programming

Before the Fin-Syn rules were in place, networks asserted ownership over prime-time programming.

> In the 1970s, what led the FCC to institute the financial interest and syndication rules was a concern that the networks were becoming both too powerful and too demanding when it came to the [program] selection process. Too powerful in that they were the gatekeepers of **news,** information, and entertainment for the American public. This was so because **of** the limits of radio spectrum... Too demanding, because networks were requiring an equity stake in a program before it would be accepted as part of the prime-time schedule.. .. [T]he networks 'had ownership of more than **70%** of their prime-time schedule by the mid-1960s, up from only **45%** the previous decade. The strong arming of producers was a fundamental reason for the creation of fin-syn.[33]

The timing is informative. TV arrives on the scene in the 1950s and becomes the dominant medium by the early 1960s. In **the** early days, broadcasters lacked both production capacity and market power to self-supply content. Once television achieved ascendance, the broadcasters used their resources and leverage to assert ownership over prime time programming.

The broadcast networks also had a history of antitrust problems in their role as gatekeepers of access to the television audience. In 1978 they lost an antitrust case that paralleled the ***Paramount*** case.

> In the *Unites States v. National Broadcasting* Co., The government specifically accused the National Broadcasting Company (NBC) **of** restraint **of** trade **as** it related to purchasing programs from independent producers and of using its

[33] Einstein, Mara, ***Media Diversity: Economics, Ownership and the*** *FCC* (Mahwah: Lawrence Earlbaum, 2004), p. 179

network power to monopolize prime-time programming production of shows broadcast on the network. The Department also claimed that NBC, with CBS and ABC, was trying to develop a monopoly over the television programming market.[34]

After a twenty-year period in which the networks were restrained by the Fin-Syn rules, the broadcasters moved to reassert ownership in prime-time programming once the rules were repealed.

Since the rules were repealled in 1995, the economic structure of the industry changed drastically. The television networks have become vertically integrated institutions with the ability to produce programming through internal business units. Corporate parents put pressure on the networks to purchase programming internally to achieve synergies and, of course, increase profits. Being part of large media conglomerates, there is added pressure on the networks to be profitable **so** that Wall Street may find the parent company appealing.[35]

The networks each have at least a 50% stake in the programming on their air and some have **as** high as **70%** and even **90%**.[36] The networks could never achieve those kinds of ownership numbers without requesting a stake in the programming that appears on their air. It is no secret to anyone that the networks do this.[37]

In the previous section I have noted the evolving pattern of behavior by the broadcasters in asserting ownership of prime time programming. Bielby and Bielby have argued that network behavior was political, as well as economic, and noted the evolving nature of their rhetoric. At first the broadcasters argued that the independents would not be squeezed out. Later they argued that independents were irrelevant.

The network executives' initial position was that independent producers would thrive in a deregulated industry and that network ownership was not a threat to creativity and program quality. Increasingly, in recent years, network executives and deregulation advocates have taken the position that their opponents' positions are irrelevant, because they are out of touch with the

[34] Einstein, **p. *60*.**
[35] Einstein, pp. 179-180.
[36] Einstein, p. 217, citing Mermigas, 2002,
[37] Einstein, p. 217.